CIFA

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On behalf of the Council of Infrastructure Financing Authorities

Subcommittee on Water Resources and Environment

Committee on Transportation and Infrastructure

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Mr. Chairman and Members of the Subcommittee:

My name is Kevin Ward and I am here today in my capacity as an Officer of the Council of Infrastructure Financing Authorities. CIFA very much appreciates the opportunity to present testimony to the Subcommittee.

CIFA is a national organization made up primarily of state officials engaged in the development and financing of water and wastewater pollution control projects and the operation of State Revolving Funds for infrastructure financing. Our members have been in the forefront of developing financial structures that maximize the use of federal and state dollars while meeting the requirements of statute, federal oversight, accountability and fiscal responsibility.

We welcome the opportunity to share our views with the Subcommittee on the financing of water infrastructure projects. It is obviously a subject to which we give a great deal of thought as we attempt, as State managers, to meet the challenge of addressing pressing needs with often limited resources.

This Subcommittee has sought in the past to increase the level of Federal support for the Clean Water State Revolving Fund and we hope that effort will continue. We believe increased funding is essential to realizing our nation's water quality goals. We also share your interest in pursuing different options and innovations that will make the best possible use of that funding. One of the primary roles of CIFA has been to facilitate the sharing of information among the States about how to run SRF programs more effectively and meet new challenges and opportunities.

Following the adage, "If it ain't broke, don't fix it" we hold strongly to the view that the State Revolving Loan Funds should remain the foundation for future progress in meeting water infrastructure needs. Innovation, new approaches and new priorities can and should be addressed in the context of the SRF concept. It is vital that the SRF partnership between federal and state government continue as the basic mechanism for assistance to communities in addressing water quality issues.

In the past two decades, few federally authorized programs have proven as effective in realizing their intended goals as the CWSRF. The CWSRFs have provided a sustainable source of funding to protect and restore our nation's rivers and streams. The assistance made available to communities is more than double the federal investment as a result of state match, loan repayments, issuance of bonds and interest earnings.

The numbers tell the story. EPA's 2004 Annual Report of the CWSRF program indicates assistance provided between 1988 and 2004 was $47.9 billion, funding a total of 15,286 projects. SRF loans save recipients 20% on average which means that communities saw a reduced cost of approximately $17.5 billion in interest charges between 1991 and 2004 due to below-market interest rates in the CWSRF program. For a typical $10 million project with a CWSRF loan, the saving is $3.2 million.

The majority of funding goes to the highest priority projects that clean up polluted streams, rivers, lakes and estuaries. CWSRF assistance primarily finances projects addressing the safeguarding of public water supplies, restoration of fish habitats and expanding recreational opportunities.

States, as the recipients of CWSRF capitalization grants, recognize that they incur a number of responsibilities. We must manage those funds in a fiscally responsible manner and be accountable. We must give priority in our funding decisions to the water quality benefits that will result and the urgency of environmental problems needing resolution. We need to give particular attention to the challenges faced by small and rural and disadvantaged communities. And, we must be creative financial stewards seeking to identify every appropriate avenue for delivering as much assistance as feasible to communities and ensuring that this assistance achieves the fullest potential impact in terms of improved water infrastructure.

We see our mission as using all the possible tools and strategies, allowable by law and consistent with prudent financial management, to achieve the largest "foot print" in terms of achieving the goals of the Clean Water Act. In the broadest sense of the term, States, whether issuers of bonds or not, are "leveraging" the resources at their disposal to maximize the federal CWSRF dollar.

Currently, 27 States take advantage of the capacity within the SRF to leverage the funds. Using that term now in the traditional financial sense, States employ the federal capital grants, as well as their matching share, as collateral to borrow in the bond market for purposes of increasing the pool of available funds for project lending. This is a very useful tool for States facing loan demand that outpaces available capitalization grants. When combined, SRF cap grants and borrowed funds can significantly increase near term loan capacity and allow more projects to be funded sooner. Leveraging the SRF has dramatically increased the funds available for assistance.

Let me provide a couple of examples of what has been accomplished in that regard.

In Massachusetts, the SRF was established as a leveraged program back in the late 1980's with the Federal grant dollars and the State match dollars being leveraged in the tax-exempt bond market. The initial leveraging ratio for the program was 2 to 1, meaning that for every $1 of grant money received, $2 was raised on the open market for project funds. Currently, Massachusetts leverages at a ratio of 3 to 1.

Since 1989, Massachusetts has received $798 million in Federal funds and contributed $175.4 million in state matching dollars for a total of $973.4 million available for projects. Through leveraging, Massachusetts has been able to issue more than $2.7 billion in construction/project loans to local governmental units, funding almost 900 projects. This assistance has financed projects across the full range of categories allowed under EPA regulations. These have included secondary and advanced treatment; inflow and infiltration; sewer rehabilitation; collection systems; interceptors; CSO's; storm water, and other non-point source type projects.

Oklahoma is a State that has only recently moved to the leveraging process. The Oklahoma Water Resources Board began leveraging in 2003 when the demand for funding from communities was rapidly exceeding the funds available from capitalization grants and state match. The first leveraged SRF transaction was in the drinking water program for $127 million. This was followed by a second transaction in which clean water, drinking water and state match bonds were issued raising $216 million. Oklahoma is the first State in EPA Region 6 to leverage the drinking water program and the first state to cross-collateralize its clean water and drinking water programs. The OWRB has further stretched these SRF bond funds by combining them with state program loan and grants, along with funding through Rural Development, Community Development Block grants, State and Tribal Assistance grants, Indian Health Service grants as well as other sources.

Both these examples illustrate States maximizing use of Federal dollars to meet water quality needs as quickly as possible with available resources.

In addition to the leveraging of SRF funds through the bond market, States are leveraging their assets in the larger sense of the word: marshaling resources, integrating funding, and accessing other sources of support to stretch the SRF dollar and finance more water infrastructure projects.

Rural states with small populations face particular challenges. Wastewater infrastructure is expensive but necessary for small communities and often several funding sources must be tapped to pay for one project. The State of Montana has been very active in addressing the rural/small community challenge. The Montana State Revolving Fund program worked with other Federal funding agencies such as the Community Development Block Grant program, USDA Rural Development and other State agencies to produce a single application process which is used to apply for all the state and federal loans and grant programs. This is of tremendous benefit to communities with limited staff resources and expertise. Montana "markets" the advantages of this integrated funding approach to communities as they begin the process of addressing their water infrastructure needs. The State program has even produced an educational video that is shown at town council and public meetings so communities can better understand their options and the process involved.

In my State of Texas we aim for the largest footprint from the use of Clean Water SRF dollars to produce the optimal impact in terms of services provided. In the case of the City of Eagle Pass, a $17,340,000 CWSRF loan was combined with EPA grants through both the Colonia Wastewater Treatment Assistance Program (CWTAP) in the amount of $18.4 million and $4 million through the North American Development Bank, along with a state grant of $2.4 million. The combined funds were used for the construction of upgraded and expanded wastewater treatment, interceptor capacity, a reuse system and new service to replace failed septic systems in colonias and a Kickapoo Tribal Reservation. This has allowed the City to become a regional service provider that will serve over 50,000 residents through a project that ensures sustainable compliant wastewater treatment capacity for a rapidly growing community and brings first time wastewater service to 2,700 homes.

Another successful Texas project that demonstrates the benefits of leveraging CWSRF appropriated dollars is the City of Roma. In Roma's case, a $4.2 million CWSRF loan was combined with $29.6 in funding from various state and federal agencies ($20.5 million EPA grant program through the CWTAP program; $1.7 million grant from the Office of Rural Community affairs (HUD); $.5 million through the USDA Rural Development program; $5.6 million EPA grant through the North American Development Bank and a state grant of $1.3 million) to realize a $33.8 million funding package. This enabled the City to construct a new wastewater plant, expand its collection system and replace inadequate on-site systems. In addition to providing compliant service to the City's 20,000 residents, the project brings first time service to approximately 2,764 economically distressed homes representing 14,000 residents.

States are also "leveraging" resources to address water quality beyond what is contemplated or required by the Clean Water Act. States have taken ownership of their respective water agendas to achieve the most comprehensive response to water quality needs. For States, improving water quality is a response not only to Federal law; it is a response to a priority concern of their citizens.

An illustration of this type of State initiative is the Community Septic Management Program administered by the Massachusetts Water Pollution Abatement Trust, the state SRF agency. This program is designed to rehabilitate or replace failing, on-site septic systems. Using $30 million appropriated by the state legislature and leveraging the funds on a 2 to 1 basis, $60 million is being provided for the remediation of septic systems. Already over 5,000 on-site systems have been rehabilitated.

Ohio is demonstrating the versatility of the CWSRF. Ohio has developed a way to use CWSRF loans to encourage improvements that will maintain and restore aquatic life in water bodies impacted by non point source pollution. In the last five years, their SRF has funded the protection and restoration of over 69 miles of stream corridors and 4,200 acres of wetlands. Ohio has also pioneered the use of linked deposit financing for the

CWSRFs. With this funding mechanism, SRFs can provide below-market interest rates through local lenders so that private borrowers can carry out a wide variety of non point source pollution controls. The Ohio CWSRF has saved those borrowers over $3.8 million by investing in more than 1,000 loans that implemented agricultural best management practices for water quality and improved home sewage treatment systems.

As the Subcommittee weighs the future of SRF reauthorization legislation, as well as other initiatives to spur water infrastructure development, we would hope that you will keep the record of accomplishment by States and the perspective of State program managers uppermost in your consideration. If progress is to continue, it will be in the hands of each individual State to deliver on the goals of the Clean Water Act.

Our organization shares this Subcommittee's concern with the far-reaching implications of the current status of FY '06 appropriations for the Clean Water State Revolving Funds. With the significant reduction in funding experienced in FY '05 and the drastic cut proposed in this year's Budget, the future of the CWSRF is at a critical juncture. With the documented huge need for water infrastructure, which will only escalate in the future, if this Subcommittee desires that the CWSRF continues to be the primary tool for Congress to ensure the states are maintaining an appropriate pace in addressing priority needs consistent with the Clean Water Act, then full consideration will have to be given to appropriate funding levels to accomplish that task. This organization is prepared to assist the committee in any way to ensure Congress is fully aware of the impacts of various funding levels on the CWSRF program.

We have long sought SRF reauthorization legislation and CIFA endorsed H.R. 1560 in the past Congress. Reauthorization of the CWSRF at significantly higher funding levels is, of course, a very important component of increasing the flow of SRF loans to meet the demand for projects. Our support for reauthorization has been somewhat tempered by efforts to use the legislation as a vehicle for imposing new requirements and obligations on the States. After years of successful program operation it is clearly the experience of CIFA State members that the more latitude and operating flexibility the States are allowed, the greater is our ability to accomplish the environmental and financial goals of the program. Certainly States need to be fully accountable for their use of federal dollars but excessive oversight or administrative control by EPA stifles innovation and the ability of States to best respond to local needs. The success of this program derives from the flexibility of the SRF model that allows each State to decide the best approach to meet its individual water quality needs. Efforts to mandate certain approaches or set aside funding for particular types of projects fail to recognize that water quality needs vary and States are in the best position to decide priorities consistent with statute.

Among the specific items we would like to see included in CWSRF reauthorization legislation are the continued ability to transfer funds between the CWSRF and the DWSRF; extended loan terms to the useful life of the project; provisions for assistance to disadvantaged communities parallel to the drinking water program and loan fee language as was contained in H.R. 1560 of the last Congress.

While we are certainly aware that tax legislation is no more this Subcommittee's purview than are appropriations bills, we do want to point out two issues in the tax arena that could significantly impact the SRF program.

As was recognized in H.R. 1560, a change in arbitrage rebate rules could make available significant additional funds for States that operate leveraged SRF programs. These States are currently forced by the arbitrage rules to limit and pay rebate on their earnings on those portions of the SRF funds which are considered under these rules to be bond proceeds. This reduces the resources available to provide financial assistance to communities. Applying the arbitrage rules in the case of SRFS does not make sense since by law these funds can only by used for the purpose of financing water and wastewater facilities and prompt lending is ensured by oversight and program audits by the EPA. Fixing this either by legislation or administrative action by the Treasury Department could mean a good deal more money for water infrastructure without additional appropriations.

In turn, leveraged State SRF programs would be negatively affected should Congress move to adopt some of the municipal bond provisions contained in the recent Joint Committee on Taxation report, "Options to Improve Tax Compliance and Reform Expenditures." Provisions in the report pertaining to tax-exempt financing may increase federal tax revenues but would constrain the ability of States to issue bonds, force significantly higher borrowing costs, and thus limit financing available for infrastructure.

Chief among the concerns are the recommendations to eliminate advance refunding and greatly restrict pooled financing. If SRF programs are caught up in these proposed bond restrictions it will limit our ability to augment assistance to communities with no benefit to the Federal Treasury. We hope the Subcommittee will keep this potential impact in mind should the tax-writing committee move in this direction.

Mr. Chairman, we very much appreciate the opportunity to share our views and look forward to continue working with you, Representative Johnson and the members of the Subcommittee as you address how best to finance the water infrastructure needs of this nation.